Webinar

Automotive Fleet & Leasing Association

Management of Employee-Provided Vehicles: *Understanding the Differences Between Reimbursement Methods*

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Background Info

- Most companies utilize two types of fleet vehicles
  - Company-provided vehicles
  - Privately-owned vehicles (POVs)
- Well-run organizations use both types of vehicles after considering all quantifiable and non-quantifiable costs and factors
- Differences between taxable and non-taxable POV reimbursement methods are often overlooked

What You Will Learn

1. Differences between taxable and non-taxable reimbursement plans
2. Fairness of using the IRS Standard Per-Mile Rate
3. Key elements of an IRS Accountable Plan, including the FAVR (fixed and variable rate) template
4. Benefits of a centralized fleet program
5. Risk management considerations

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“Non-Accountable” Taxable Plan

- Taxable Plans
  - Cents-per-mile (CPM) that exceeds **reasonableness** standards accepted by the IRS
  - Flat dollar allowances
  - Some fixed and variable allowances
- What Happens
  - Income is included in employee’s W-2 statement
  - Employee potentially deducts cost from personal income tax
- Advantages
  - Simplifies administrative procedure
- Disadvantages
  - Both employer and employee pay taxes
    - Withholding
    - FICA
    - Federal and state unemployment
  - Employee’s interest cost to fund a POV is not tax deductible

Negative Tax Consequences

$500 Monthly Allowance = $6,000 Annual Tax Base

Tax Description	Employer	Employee
Social Security (6.20%/6.20%)	$372	$372
Medicare (1.45%/1.45%)	$87	$87
Federal @ 30%[1]	N/A	$1,800
State @ 6% [1]	N/A	$360
Annual Incremental	**$459**	**$2,619**
Monthly Incremental	**$38**	**$218**

[1] Average

Monthly Allowance After Tax

Allowance $500 − Taxes $218 = Net $282

Business Tax Deduction

- Must itemize deductions
- Must meet threshold of 2% Adjusted Gross Income to deduct (more if joint return)
- If applicable, Alternative Minimum Tax disallows deduction of "employee business expense"

Fairness of Using the IRS CPM Rate

Flat $0.56 CPM rate is inequitable **when travel or expense patterns vary**

Driver A

- Territory = high density, small area
- 12,000 annual miles = $6,720 gross reimbursement
- $1,720 after $5K fixed ownership
- **Net $0.14 CPM**

Driver B

- Territory = long distance between calls, large area
- 24,000 annual miles = $13,440 gross reimbursement
- $8,440 after $5K fixed ownership
- **Net $0.35 CPM**

Assumptions

Both drivers pay $5,000 fixed ownership cost per year for the same:

- Employer
- Community
- Vehicle
- Insurance coverage/cost
- Misc. expense (tax, registration)

Key Elements – IRS Accountable Plan

- Broad guidelines for calculating and documenting non-taxable vehicle allowances and reimbursements to substantiate expense:
  - Amount
  - Time
  - Place
  - Business purpose

- Plan Requirements
  1. Geographic-specific fixed and variable costs
  2. Customized by driver or group
  3. Combine a flat dollar amount (based on ownership costs) with a per-mile reimbursement (derived from actual operating costs)

Required Criteria to be Tax-Free

1. Business Connection

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Must

- Be **reasonably** calculated
- Not exceed anticipated expenses
- Be provided on uniform and objective basis
- Be periodically paid at a fixed and variable rate
- Be consistently applied in accordance with **reasonable** business practices

- Employee required to return any excess reimbursements over substantiated expenses within a **reasonable** period of time (120 days)

IRS FAVR Accountable Plan Template

- Fixed and Variable Rate
  - FAVR is **not** mandatory
  - Requires specific guidelines and data elements
  - Has 21 data, program, and driver tests
  - Management is often outsourced to consulting firms due to rigid framework
- Specific Data Elements
  - Insurance
  - Vehicle age
  - Vehicle value
  - Minimum mileage
  - Business use percentage
  - Enrollment
  - Management employee enrollment limits

Accountable Plan Differences

Key Elements/Test Criteria	FAVR	Non-FAVR
Basis for Calculation	Fixed and variable rate, based on geographic cost differences relative to vehicle standards	Fixed and variable rate, based on geographic cost differences relative to vehicle standards
Taxability	Presumed non-taxable if FAVR-specific criteria are followed to the letter (21 data, program and driver tests); must provide documentation of compliance	Justified as non-taxable by substantiating business use and structuring payments as reimbursements
Justification to Ensure Non-taxable Status	Drivers must provide verification of vehicle age, insurance coverage, percent of business and personal use	Drivers report business miles/ verify expenses; can fallback on IRS mileage reimbursement safe harbor and report any over payment as taxable
Key Benefit	Program criteria pre-approved by IRS	More flexibility in calculation and justification criteria
Biggest Drawbacks	Highly restrictive criteria, limited executives allowed in program, drivers may fall out of compliance and not know until too late	"Reasonableness" standards may need to be defended in case of audit

Why Have a Centralized Fleet Program?

- Fleet manager is the ideal candidate for authority over both company-provided vehicles and POVs
- Numerous commonalities under both strategies
  - Negligence
  - Vicarious liability
  - Productivity
  - Compliance with Sarbanes-Oxley
    - Non-compliance with IRS rules will likely indicate non-compliance with SOX
    - Obtain certificate of SOX compliance from POV consulting firms and validate through standard auditing practices

Risk Management Considerations

True or False?

"Most fleet accidents occur during personal use."

- U.S. Vehicle Statistics
  - 253.6M registered vehicles[1]
  - 211.0M licensed drivers[2]
  - ~20% fleet drivers = 42M
  - NHTSA
    - Most crashes occur 3-9pm with majority 6-9pm **because more vehicles are on the road**
    - Most fatalities occur **late night and are alcohol related**

- Apples and Oranges
  - General population drives greater % personal use than fleet
  - Fleet drivers have lower crash rates than general population[3]
- Majority of fleet crashes occur during **business**
  - TRW 10-year study
  - Nationwide Insurance
  - NAFA

1. Passenger cars, motorcycles, trucks, buses, and other vehicles. Statista.com. U.S. DOT. 2012.
2. U.S. Census Bureau, Statistical Abstract of the United States: 2012.
3. Network of Employers for Traffic Safety. NAFA Fleet Management Association.

Risk Management Considerations

POV Risk is Consistent With Company-Provided Vehicles

- Negligence
  - Entrustment
  - Retention
  - Hiring
  - Supervision
- Vicarious Liability

- How to Mitigate POV Risk
  - POV safety policy
  - MVRs
  - Insurance: $300K business coverage with financially solvent insurer
  - Named additional insured
  - Properly maintained and safe vehicles
  - Safety training and education

Summary

- ✓ Review negative tax consequences of taxable reimbursement plans
- ✓ Understand how to calculate and document non-taxable vehicle allowances
- ✓ Practice centralized management of company vehicles and POVs
- ✓ Consider risk management issues

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QUESTIONS AND ANSWERS